

**Franchise Tax Board****ANALYSIS OF ORIGINAL BILL**

Author: Plescica Analyst: Raul Guzman Bill Number: AB 2037  
Related Bills: See Legislative History Telephone: 845-4624 Introduced Date: February 14, 2006  
Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Public School Extracurricular Activity Contributions Or Fees Credit

**SUMMARY**

This bill would create a credit for contributions made or fees incurred to support a public school's extracurricular activities.

**PURPOSE OF THE BILL**

According to the author's office, the purpose of this bill is to support the extracurricular activities at public schools.

**EFFECTIVE/OPERATIVE DATE**

This bill is a tax levy and would be effective immediately upon enactment. The credit would be operative for taxable years beginning on or after January 1, 2006.

**POSITION**

Pending.

**ANALYSIS****FEDERAL/STATE LAW**

Current federal and state tax laws provide various tax credits designed to provide tax relief for taxpayers that incur certain expenses (e.g., child and dependent care credits) or to influence business practices and decisions or achieve social goals.

Current federal and state tax laws allow a taxpayer to claim charitable contributions as an itemized deduction. Deductions are allowed for monetary charitable contributions or gifts of property to: qualified federal, state, or local governments, or to organizations formed for religious, charitable, educational, scientific, or literary purposes, or for the prevention of cruelty to children or animals.

Board Position:

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_____ N	_____ OUA	_____ <u>X</u> PENDING

Department Director

Date

S. Stanislaus

5/10/06

A charitable contribution is defined as a contribution or gift made exclusively for public purposes. A taxpayer is allowed to subtract the greater of the standard deduction or itemized deductions from adjusted gross income (AGI) to calculate taxable income.

Under federal and state laws, the deductible amount of any charitable contribution may be reduced depending on the type of contributed property, the organization to which the property is contributed, and the income of the taxpayer. Generally, the amount of any deduction for contributed property that would have resulted in ordinary income being recognized had the property been sold is limited to the property's basis.

Current federal and state tax laws place limitations on charitable contributions. The limitations vary from 20%, 30%, or 50%, depending on the individual's AGI and the amount of contributions made, the types of organizations that receive the donations, and the type of property donated. If an individual's charitable contributions are limited, the excess may be carried over for five years.

### THIS BILL

This bill would provide two credits, a credit for contributions made and a credit for fees incurred by a taxpayer for support of California public school extracurricular activities.

This bill would place the following caps on the amount of the credit allowed:

- \$200 for individuals and head of household, a maximum \$150 for married filing separate, and a maximum \$300 for married filing joint taxpayers for taxable years beginning January 1, 2006.
- \$400 for married filing joint taxpayers, and \$200 for married filing separate taxpayers for taxable years beginning January 1, 2007.

Extracurricular activities are defined as school sponsored events or activities that require a fee to be accrued by an enrolled student.

This bill would include the following restrictions on qualifying contributions:

- The credit would exclude contributions designated for the benefit of a specific student.
- The contribution may not be allocated by the school to pay salaries of any kind.
- Contributions made under this bill are meant to augment rather than replace any existing public funding for extracurricular activities.

This bill would allow any credit that exceeds the taxpayer's tax liability to be carried over and used in the following six years.

This bill would further provide that a school that receives a contribution would be required to provide the taxpayer with a receipt and make available to the public an annual report on the total amount of contributions and their use.

## IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

This bill would treat fees incurred differently than contributions made. Namely, limitations would apply only on contributions made. For example, fees collected could be used to pay salaries, other expenses, or augment a school's budget. The author may wish to amend the bill to impose the same limitation on fees as would be imposed on contributions.

This bill would allow a credit for fees incurred, rather than fees paid. As a result, if a taxpayer's dependent participated in extracurricular activities and fees were incurred, the taxpayer would qualify for the credit regardless of whether the fee was actually paid.

"Public school" lacks a definition. Under this bill, public school could be interpreted to include all public schools ranging from elementary to college. The author may want to amend the bill to clarify which types of schools would qualify for the credit.

The definition of "extracurricular activities" is broad. Under the current definition, extracurricular activities could be interpreted to include, but not be limited to, activities such as fraternity and sorority parties, adult education programs, and parent teacher associations. The author may wish to amend the bill to more narrowly define extracurricular activities.

This bill would provide a more generous credit to single persons. Married filing joint taxpayers would be allowed a \$300 credit while single taxpayers would be allowed a \$200 credit.

This bill excludes a filing status for qualifying widow(er). Generally, credits are allowed to qualifying widow(er) in the same amount as married filing joint taxpayers. The author may wish to amend the bill to include the "qualifying widow(er)" filing status.

To verify that a contribution or fee meets the credit requirements upon audit, the department would recommend including a requirement that the taxpayer provide a receipt upon request and that the recipient school include the following information on the receipt:

- The school's name.
- The taxpayer's name.
- The date and amount of donation.
- A statement that the funds will be used for a qualifying activity or an extracurricular activity.
- A statement that the taxpayer did not designate that the contribution be used for a specific student or a dependent of the taxpayer.

This bill fails to provide any consequence for a school that uses a contribution for salaries, other expenses, or supplement to its budget. The author may wish to amend the bill to include language that would provide consequences for such actions.

## TECHNICAL CONSIDERATIONS

Minor operative date errors were found. Amendments have been provided to correct the errors.

## **LEGISLATIVE HISTORY**

AB 1625 (Pescetti, 2001/2002) and AB 122 (Kaloogian, 1999/2000) would have allowed a tax credit for contributions or fees paid to a public school to support its extracurricular activities. Both bills failed passage out of the Assembly Revenue and Taxation Committee.

## **OTHER STATES' INFORMATION**

Review of *Illinois, Massachusetts, Michigan, Minnesota, and New York* laws found no comparable tax credits. These states were reviewed because of the similarities to California income tax laws.

## **FISCAL IMPACT**

Once the implementation considerations are resolved, the department's costs to implement this bill are expected to be minor.

## **ECONOMIC IMPACT**

### Revenue Estimate

Based on data and assumptions discussed below, the revenue loss from this bill would be as follows:

Estimated Revenue Impact of AB 2037 Effective On Or After January 1, 2006 Enactment Assumed After June 30, 2006 (in Millions)			
Fiscal Year	2006-07	2007-08	2008-09
Revenue Loss	-\$455	-\$595	-\$615

This estimate does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

### Revenue Discussion

Revenue losses would be determined by the number of taxpayers paying fees for activities sponsored by qualified public schools, the amount of the fees, and the tax liabilities of taxpayers.

According to data from the Department of Finance, the number of students enrolled in California public schools in grades K-12 was approximately 6.3 million in the 2004/05 school year. These students are assumed to be the dependents of about 3.2 million taxpayers.

The estimate assumes that 70% of taxpayers (3.2 million times 70% equals 2.2 million taxpayers) would claim the proposed credit during the school year for students' participation in qualified activities. This number was increased 20% to include non-parent contributors; bringing total taxpayers to 2.6 million (2.2 million increased 20% is 2.6 million).

An average contribution of \$175 was assumed in the first year, increasing to \$225 in the second year due to the credit increase permitted to married filing joint taxpayers. The number of taxpayers and the dollar amounts were grown annually by school enrollment growth rates, and by 3.2% annual inflation rate, respectively. The estimate above is calculated as 2.6 million taxpayers times \$175 equals \$455 million.

## **POLICY CONCERNS**

With regard to the Extracurricular Activities Credit, conflicting tax policies come into play whenever a credit is provided for an item that is already deductible. Generally contributions to public schools and charitable organizations are deductible. This bill would have the effect of providing a double benefit by creating a credit and allowing the full amount to be deducted. If the author's intent is to allow a double benefit, no additional language is needed. However, if the author's intent is to allow only one tax benefit or the other, then additional language is needed.

It is not clear what the author's intent is with respect to the following issues:

1. This bill would only allow individuals to claim the credit; it does not allow other taxpayers or entities to claim the credit.
2. If a taxpayer is entitled to both credits, one for contributions and the other for fees incurred, can a taxpayer claim two separate maximum amounts?

This bill lacks a sunset date. Sunset dates generally are provided to allow periodic review by the Legislature.

## **LEGISLATIVE STAFF CONTACT**

Raul Guzman  
Franchise Tax Board  
845-4624  
[raul.guzman@ftb.ca.gov](mailto:raul.guzman@ftb.ca.gov)

Brian Putler  
Franchise Tax Board  
845-6333  
[brian.putler@ftb.ca.gov](mailto:brian.putler@ftb.ca.gov)

Analyst	Raul Guzman
Telephone #	845-4624
Attorney	Patrick Kusiak

FRANCHISE TAX BOARD'S  
PROPOSED AMENDMENTS TO AB 2037  
As Introduced February 14, 2006

AMENDMENT 1

Page 1, line 3, strikeout "on and after" and insert:  
on or after

AMENDMENT 2

Page 2, line 5, after "2006," insert:  
and before December 31, 2006,